APPENDIX

Revenue Act of 1934, c. 277, 48 Stat. 680:

SEC. 23. DEDUCTIONS FROM GROSS INCOME.

In computing net income there shall be allowed as deductions:

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(m) *Depletion.*—In the case of mines, oil and gas wells, other natural deposits, and timber, a reasonable allowance for depletion and for depreciation of improvements, according to the peculiar conditions in each case; such reasonable allowance in all cases to be made under rules and regulations to be prescribed by the Commissioner, with the approval of the Secretary. In any case in which it is ascertained as a result of operations or of development work that the recoverable units are greater or less than the prior estimate thereof, then such prior estimate (but not the basis for depletion) shall be revised and the allowance under this subsection for subsequent taxable years shall be based upon such revised estimate. In the case of leases the deductions shall be equitably apportioned between the lessor and lessee. In the case of property held by one person for life with remainder to another person, the deduction shall be computed as if the life tenant were the absolute owner of the property and shall be allowed to the life tenant. In the case of property held in trust the allowable deduction shall be apportioned between the income beneficiaries and the trustee in accordance with the pertinent provisions of

the instrument creating the trust, or, in the absence of such provisions, on the basis of the trust income allocable to each. * * *

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SEC. 114. BASIS FOR DEPRECIATION AND DEPLETION.

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(b) *Basis for Depletion.*—

(1) *General rule.*—The basis upon which depletion is to be allowed in respect of any property shall be the adjusted basis provided in section 113 (b) for the purpose of determining the gain upon the sale or other disposition of such property, except as provided in paragraphs (2), (3), and (4) of this subsection.

(2) *Discovery value in case of mines.*—In the case of mines (other than metal, coal or sulphur mines) discovered by the taxpayer after February 28, 1913, the basis for depletion shall be the fair market value of the property at the date of discovery or within thirty days thereafter, if such mines were not acquired as the result of purchase of a proven tract or lease, and if the fair market value of the property is materially disproportionate to the cost. The depletion allowance under section 23 (m) based on discovery value provided in this paragraph shall not exceed 50 per centum of the net income of the taxpayer (computed without allowance for depletion) from the property upon which the discovery was made, except that in no case shall the depletion allowance under section 23 (m) be less than it would be if computed without reference to discovery value. Discoveries shall include minerals in commercial quantities contained within a vein or deposit discovered in an existing mine or mining tract by the

taxpayer after February 28, 1913, if the vein or deposit thus discovered was not merely the uninterrupted extension of a continuing commercial vein or deposit already known to exist, and if the discovered minerals are of sufficient value and quantity that they could be separately mined and marketed at a profit.

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Treasury Regulations 86, promulgated under the Revenue Act of 1934:

ART. 23 (m)–1. *Depletion of mines, oil and gas wells, other natural deposits, and timber; depreciation of improvements.*—* * *

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When used in these articles (23 (m)–1 to 23 (m)–28) covering depletion and depreciation—

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(c) A "mineral deposit" refers to minerals only, such as the ores only in the case of a mine, to the oil only in the case of an oil well, and to the gas only in the case of a gas well, and to the oil and gas in the case of a well producing both oil and gas. The cost of a mineral deposit is that proportion of the total cost of the mineral property which the value of the deposit bears to the value of the property at the time of its purchase.

(d) "Minerals" include ores of the metals, coal, oil, gas, and such nonmetallic substances as abrasives, asbestos, asphaltum, barytes, borax, building stone, cement rock, clay, crushed stone, feldspar, fluorspar, fuller's earth, graphite, gravel, gypsum, limestone, magnesite, marl, mica, mineral pigments, peat, potash, precious

stones, refractories, rock phosphate, salt, sand, silica, slate, soapstone, soda, sulphur, and talc.

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ART. 23 (m)–14. *Discovery of mines other than coal, metal, or sulphur mines.*—(a) To entitle a taxpayer to a valuation of his property, for the purpose of depletion allowances, by reason of the discovery of a mine (other than a coal, metal, or sulphur mine) or minerals (other than oil or gas, coal, sulphur, metal, or metallic ores), it must appear that the mine or minerals were not acquired as the result of the purchase of a proven tract or lease; also, the discovery must be made by the taxpayer after February 28, 1913, and must result in the fair market value of the property becoming disproportionate to the cost. The fair market value of the property will be deemed to have become disproportionate to the cost when the newly discovered minerals are of such quantity and of such quality as to afford a reasonable expectation of return to the taxpayer of an amount materially in excess of the capital expended in making such discovery plus the cost of future development, equipment, and exploitation.

(b) A mine or minerals of a kind not excepted by this article may be said to be discovered when (1) there is found a natural deposit of mineral, or (2) there is disclosed by drilling or exploration, conducted above or below ground, a mineral deposit not previously known to exist and the existence of which was so improbable that such deposit had not and could not have been included in any previous valuation for the purpose of depletion, and which in either

case exists in quantity and grades sufficient to justify commercial exploitation.

(c) In determining whether a discovery entitling the taxpayer to a valuation has been made, the Commissioner will take into account the peculiar conditions of each case; but no discovery, for the purposes of depletion, can be allowed as to minerals which constitute merely uninterrupted extensions of continuing commercial veins or deposits already known to exist, which have been or should have been included in "probable" or "prospective" mineral, or which were in any other way comprehended in a prior valuation, nor can a discovery, for purposes of depletion, be allowed as of a date subsequent to that when, in fact, discovery was evident, when delay by the taxpayer in making claim therefor has resulted or will result in excessive allowances for depletion.

(d) Discoveries include minerals in commercial quantities contained within a vein or deposit discovered in an existing mine or mining tract by the taxpayer after February 28, 1913, but such vein or deposit must not be merely the uninterrupted extension of a continuing commercial vein or deposit already known to exist, and the newly discovered minerals must be of sufficient value and quantity that they could be separately mined and marketed at a profit.

(e) The value of property claimed as the result of a discovery must be the fair market value, as defined in article 23 (m)–7, based on what is evident within 30 days after the commercially valuable character and extent of the discovered deposits of mineral have with reasonable certainty been established, determined, or proved.

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